

Service outsourcing and its effects on knowledge

ANDERS RICHTNÉR, Assistant Professor

Stockholm School of Economics, Centre for Innovation and Operations Management,
P.O. Box 6501, SE-113 83 Stockholm, Sweden

E-mail: anders.richtner@hhs.se,

JON ROGNES*, Assistant Professor

(*Corresponding author)

Stockholm School of Economics, Centre for Innovation and Operations Management,
P.O. Box 6501, SE-113 83 Stockholm, Sweden

E-mail: jon.rognes@hhs.se

Bibliograph

Anders Richtnér is Assistant Professor at the Stockholm School of Economics and has previously been a visiting fellow at Politecnico di Milano and the University of Cape Town. He received the best paper award at the IPDMC conference in 2002, and the EFMD/Emerald Outstanding Doctoral Award in Operations Management and Supply Chain Management in 2006. He has published in journals such as the *International Journal of Innovation Management*, *International Journal of Operations and Production Management*, *Journal of Product Innovation Management*, and *Research Policy*.

Jon Rognes holds a Ph.D. from Stockholm School of Economics in Business Administration (1999). At the moment he holds a position as Researcher at the Center for Management and Organization at Stockholm School of Economics. Active research projects are: Outsourcing and offshoring of services, focusing on organisational impact of centralisation / relocation of service functions, Lean Services, and the application of Lean Production principles on mass production of services. 2004-05 visiting professor at Asian Institute of Management, Manila. 2000 - 2001 Associate visiting Scholar at Stanford University, California. Previous projects: Telecommuting, organisational impact of home based telecommuting. Global R&D units, the use of global teams in R&D. Dr Rognes also teaches Operations strategy and Operations management.

Title: Service outsourcing and its effects on knowledge

Purpose:

The purpose of the paper is to identify changes in different types of knowledge in a service outsourcing relationship as knowledge is transferred from the client to the provider, which correspond to the research question that guides the paper: ‘What are the effects on knowledge types when parts of service production are outsourced to a third party and knowledge is transferred?’. To answer this question we explored changes in both tacit and explicit knowledge taking place in several service outsourcing relationships.

Design/methodology/approach

A case study approach is chosen, as data is obtained from multiple levels. We studied four service outsourcing relationships, with outsourcing providers and outsourcing clients based in Europe and South-east Asia. Our main source of information was semi-structured interviews.

Findings

It is possible to identify two major changes as service outsourcing is conducted. (1) There is a change of relative importance of knowledge types; there is an increased emphasis on explicit knowledge as opposed to tacit knowledge. This is (2) caused partly due to the transfer situation and partly due to a focus on efficient mass production and a standardisation and industrialisation of the service. The focus on explicit knowledge leads to a loss of tacit knowledge.

Research limitations/implications

Our research is limited in two ways. First, we examined two countries. Thus, there are opportunities for expansion into more settings. Second, our findings can be tested by survey-type research thereby increasing the sample.

Practical implications

In a service outsourcing relationship the emphasis is most often on explicit knowledge. This is beneficial in a transaction cost relationship with standardized tasks being transferred. However, the more complex tasks being transferred the more difficult it is to clearly specify what is going to be transferred as the knowledge becomes more tacit, calling for more long-term relationships with other mechanisms for knowledge transfer of tacit knowledge in place. As a manager one need to be able to distinguish which type of relationship is wanted.

Originality/value

This paper helps to clarify what happens in a transfer situation when outsourcing is conducted. Particularly we emphasize the importance of tacit knowledge – a dimension often neglected in research – opposed to solely emphasizing explicit knowledge.

Key words

Service outsourcing, BPO, knowledge, knowledge transfer, service management

Type of paper:

Case study

Introduction

Outsourcing often follows from managers' rationale aiming at reducing costs and improving the balance sheet, leading to an overall increased competitiveness of the company (McIvor, 2000; Quinn & Hilmer, 1994). By focusing on core value-creating activities and outsourcing tasks to specialized companies implies that the client can focus on fewer activities thereby lowering cost and complexity of the own organization and also increasing efficiency of the remaining activities (Jiang et al., 2006; Harland et al., 2005).

Despite the rapid growth of practicing outsourcing, with between 10-40% annually over the last 10 years (Clegg, 2005) there are still companies not achieving expected benefits from outsourcing. For instance, Lonsdale (1999) and McIvor (2000) discuss that as low as 5 per cent of companies actually achieve significant benefits from outsourcing. Barthelemy (2001) also report several cases of failed outsourcing contracts. Reasons for failure are; an oversimplified view on the transfer of the task, lack of improvements over time, focus on achieving short-term benefits, lack of formulating and quantifying requirements (Beaumont & Sohal, 2004; Lonsdale, 1999). According to Harland et al. (2005, p. 839) *'the most significant risk lie in the need to develop new management competencies, capabilities and decision-making processes'*, which is linked to how the relationship between the client and the provider is actually handled. Thus, outsourcing clearly is not an easy win.

This paper describes a particular case of outsourcing, service outsourcing, an arrangement in which high volume, IT-dependent standard tasks are transferred from a company (the client) to a third party supplier (the provider), either domestically or offshore. Prior research on outsourcing has predominantly taking the perspective of the client company (Canez et al., 2000; Harland et al., 2005; Ulrich & Ellison, 2005). Some research are emerging taking the subcontractor perspective (Sousa & Voss, 2007), but more research is needed (Webster et al., 2000). The service area is also under-researched, with a few exceptions (e.g. Seuring, 2003; Safizadeh, 2008).

We aim in this paper to address these gaps and contributing with knowledge on why service outsourcing relationship succeeds or not. We will do this by a) taking into account both the view of the client and the provider, b) study service outsourcing. Particularly we will investigate the role of knowledge transfer for explaining why service outsourcing may be successful or not. Successful knowledge transfer is not easy to achieve, not even in the simplest cases (from unit to unit within a company), and understanding the factors contributing to successful knowledge transfer is an important area both for academics and practitioners (Easerby-Smith et al., 2008).

The paper is structured as follows: First we review the literature on outsourcing and specifically service outsourcing followed by a review of the literature on knowledge transfer. Second, we describe the research methodology, a multiple case study. Third, we describe the empirical setting and general issues. Fourth, we discuss the interrelationship between the issues. Finally, we present out overall conclusions, implications for managers, and suggestions for future research.

Theoretical positioning

The scope of literature considered relevant for studying knowledge transfer in service outsourcing is a salient point. The different views of outsourcing will shortly be recapitulated as a starting point, and then follows a review of the service outsourcing and knowledge literature.

From that we go further into the concept of knowledge, specifically knowledge transfer. From the literature review we identify gaps in the literature and gain insight into a specific set of research questions.

Different views of outsourcing

Several different views of how outsourcing should be defined exist in the literature (Gilley & Rasheed, 2000; Harland et al., 2005). We follow the definition by Beaumont & Sohal (2004, p. 689) who defines outsourcing as: *having worked that was previously done inside the organization performed by an external organization*. Thus, we take a rather strategic and holistic view of outsourcing. Perhaps more importantly than the definition of outsourcing are the key elements of outsourcing emerging from different definitions. Sousa & Voss (2007) has identified five characteristics of outsourcing; First, outsourcing implies a business relationship between two parties. Second, outsourcing is general business processes or processes' results, ranging from core activities (e.g. R&D and manufacturing), to support (e.g. IT and logistics) processes. Third, outsourcing is not a simple purchasing decision. Fourth, the outsourced objects are specific to the client. Fifth, and finally, the client may outsource all or part of a process or process result.

In this paper we focus on a specific part of outsourcing, service outsourcing, which is an arrangement in which high volume, IT-dependent standard tasks are transferred from a company (the client) to a third party supplier (the provider), either domestically or offshore. Putting our research in the terminology of Sousa & Voss the implication is that all five characteristics apply. Comparing our study to previous studies on service outsourcing we differ as we in this paper investigate the arguments from both sides, i.e. both the view of the client and the view of the provider, and that we particularly focus on knowledge transfer. However, prior going into details about why we focus on knowledge transfer it is necessary to review the literature on service outsourcing and knowledge in general.

Service outsourcing

Service outsourcing is often driven by an aim to save costs, yet it is not without difficulties. A review of studies on service outsourcing (Clegg, 2005) identifies cost savings as the major drive for considering service outsourcing and results shows a 10-20 percentage saving on measured factors. However, there are also difficulties with service outsourcing e.g. lack of cost savings due to increased management costs, reduced service quality, and finally worse working conditions.

Fanguli and Shiel (2006) discuss a possible shift from outsourcing simple tasks to the outsourcing of more complex activities, and label this knowledge process outsourcing (KPO). They note that business processes are constantly evolving and are strongly embedded in the culture and identity of the company. Such processes contain both explicit and tacit elements. In theory the explicit elements can be scripted, standardized and outsourced but the tacit elements are "learned" by absorbing the organizational culture. In practice however, both elements exist together (Fanguli and Shiel 2006). Due to the constantly evolving nature of business processes the level of understanding, communication, and trust between the company and its supplier has to be high. Their main conclusion is on communication and integrative structures, and does not include effects on knowledge itself in the involved parts.

Barthelemy (2001) also touches upon the issue of knowledge as he identifies several hidden costs in service outsourcing, which can be reduced by building a closer relationship between the client

and the provider. However, to transfer employees with in-depth knowledge of critical issues to the provider is a mistake as it will lead to loss of in-house knowledge and difficulties when changing supplier or taking the activity back in-house.

Schlosser (2006) notes that HR outsourcing can result in a significant loss in learning capital through a breakdown in the psychological contract, if outsourcing is introduced for cost control rather than strategic re-focusing reasons. Levitt and March (1988) outlined four traditional sources of organizational learning: (1) learning by direct experience; (2) interpretation of history (reflecting shared perspectives); (3) retrieval of knowledge from organizational memory (using established communication channels and routines); and (4) learning from the experience of others.

The first three sources are adversely affected by outsourcing, according to Schlosser, because the temporary nature of outsourcing weakens the traditions and routines associated with a strong organizational culture. HR is often responsible for communicating this organizational culture. However, an outsourced HR function may not be familiar with the organization's culture and, through poorly aligned recruiting practices, could eventually weaken this culture. De Long and Fahey (2000) described cultural characteristics that shaped social interaction and behaviours that leverage knowledge, including learning-oriented characteristics such as orientation to existing knowledge and expertise, knowledge sharing, teaching, and learning from mistakes. Organizations can increase knowledge and diversity through outsourcing, but this will not necessarily translate into increased organizational knowledge.

A common argument in sales material and among proponents for outsourcing is the possibility to access new knowledge in the outsourcing relationship. Feeny et al (2005) lists professional knowledge and domain expertise of the outsourcing provider as one important criterion when judging a potential provider. This is linked to competencies in two other main areas, relationship competencies and transformational competencies. Professional knowledge and domain expertise can be linked to formal and explicit knowledge, while a relationship competency is a more elusive concept. Feeny describes this as "capabilities that determine the supplier's willingness and ability to align with client needs and goals over time". Transformational competencies may have both formal components and soft aspects.

As can be seen above there are several studies examining service outsourcing and also touching upon the issue of knowledge, however not going into detail about the relationship. One reason is brought forward by Willcocks (2004), who notes that organisations have no real understanding of how knowledge is affected in outsourcing situations, and that knowledge in general and knowledge transfer in particular are crucial for the success of service outsourcing. Youngdahl & Ramaswamy (2008) extend the work by Willcocks and has developed a conceptual model over the relationship between knowledge work and service outsourcing, particularly arguing the knowledge work differs depending on task being conducted, and as a consequence the knowledge embedded in the process can range from how to low.

However, organizations still lack the means and experiential research to assign value to the knowledge they are transferring and receiving. Addressing this important gap in the literature our aim in this paper is to fill this gap and our purpose is: *to identify changes in different types of*

knowledge in a service outsourcing relationship as knowledge is transferred from the client to the provider. A salient point in answering our purpose is to identify an appropriate framework, which we will develop in the next section.

Knowledge

Research on knowledge is characterized by a wide array of theoretical perspectives, but tends to converge in the three ways (Argote, et al. 2003):

- First, knowledge management outcomes (knowledge creation, transfer, and retention). The process of knowledge creation occurs when organizations generate new knowledge. The process of knowledge transfer is when one unit is affected by the experience of another. Knowledge retention is the process of embedding knowledge in a repository so that it exhibits some persistence over time.

Of particular importance for this study is knowledge transfer, which is the process through which experience acquired in one unit affects another (Argote, et al. 2003). Knowledge transfer is important as knowledge from outside of the company can be an important stimulus for change and organizational improvement (Inkpen & Tsang, 2005). However, knowledge transfer is a complex process, and successful transfer is hard to achieve. Easterby-Smith et al. (2008) points out that the transfer of knowledge between organizations brings out more complexity due to the multifaceted nature of the boundaries, cultures, and processes involved, making it an interesting domain for further research.

- Second, the properties of the context in which knowledge management occur: properties of units (an individual, a group, or an organization).
- Third, properties of the knowledge itself, which tend to converge into the identification of two distinct types of knowledge; “explicit” and “tacit” knowledge (Gourlay, 2006). Explicit knowledge is what can be defined, measured, and documented, whereas tacit knowledge is difficult to articulate, sometimes invisible, existing on a subconscious level.

In the following the focus on what happens to the two types of knowledge (explicit and tacit) as knowledge is transferred between two distinct organization (the ‘client’ and the ‘provider’). Put differently the context which we are looking at is a knowledge transfer process between two organizations as they engage in a service outsourcing relationship, and the actual object of study is the changes in the properties of knowledge itself. Below we further elaborate on the types of knowledge.

Knowledge types

Nonaka & Takeushi (1995) stress the importance of both explicit and tacit knowledge in the knowledge creating process in companies, and describes how the tacit knowledge of employees (knowledge rooted in their experiences and values) can be transformed into explicit knowledge useful to the organization. Put differently tacit and explicit knowledge are mutually complementary entities, which interact with and interchange into each other through a social conversation process.

Lam (2000) argues that the innovative capability of an organization is dependent upon the organization’s ability to create knowledge, which involves: (1) the use and generation of tacit knowledge, and (2) the ability of an organization to mobilize tacit knowledge and foster its

interaction with explicit knowledge. It is important to note that the difference between the two is that tacit knowledge is more difficult to transfer than explicit knowledge, and the tacit dimension of knowledge is often poorly understood (Koners & Goffin, 2007).

Definition of Research Question

The purpose of the paper purpose is to identify changes in and changed relationship between different types of knowledge in a service outsourcing relationship which correspond to the research question that guides the rest of the paper:

RQ: What are the effects on knowledge types when parts of service production are outsourced to a third party and knowledge is transferred?

To answer this question we explored changes in both tacit and explicit knowledge taking place in several service outsourcing relationship.

Methodology

We selected a multiple case study methodology, based on the exploratory nature of the research, allowing us to investigate the phenomenon of interest in depth (Yin, 1994). The choice of a multiple case study helps to increase the generalization and to produce more robust results (Eisenhardt & Graebner, 2007; Yin, 1994, pp. 45-46).

Sample selection

The sampling frame was to include both clients and providers i.e. we wanted to have cases representing both views. The companies were selected from two counties (one from Northern Europe, and one from South East Asia). The first criterion for selecting a case was that each studied cases should be actively involved in BPO-related activities today. Second, the cases should deal with service outsourcing, from our previous discussion it implies that high volume, IT-dependent standard tasks are transferred to a third party supplier, either domestically or offshore. Third, we also considered size and chose cases focusing large clients (multinational companies) and large providers (more than 100 employees). Taking into consideration availability and access to cases we choose to study four service outsourcing relationships, corresponding to 8 cases. The company names are not disclosed to preserve anonymity at the request of our case-companies. Table 1 summarizes the cases.

INSERT TABLE 1 ABOUT HERE

Data collection

Data were primarily collected through semi-structured interviews with managers and line personnel of the client and the provider. In total we performed 50 interviews, out of these 40 interviewees were in management positions, and the remaining 10 in production units. The interviews ranged between ½ hour to 2 hours. The interviews followed a semi-structured character.

Examples of questions are the following: How do you cooperate with supplier/client? How is daily communication managed? How often and in what way do you communicate with your client/supplier? How is the transfer process handled when a new relation is started? How do you decide what to outsource (client)? What problems/challenges have you encountered? How have you solved these problems/challenges? Are there any changes over time in work content or relations with supplier/client? How do you resolve problems between you and your client/supplier? How do you share knowledge/new insights/improvements?

We also had access to written information from the cases, which was used to cross-check the information in the interviews.

Data reduction and analysis

The reduction and analysis of data was conducted in two different stages

- *Within-case analysis.* For each case data was analyzed to give a comprehensive understanding of each of the cases. At the outset we starting with no preset categories, and by iterating and recoding the material finding recurring themes (Locke, 2001). After this first analysis, conducted with the help of various sorting tools such as dedicated computer software and simple tables were use, we used the same framework for each of the cases, i.e. thematic sorting and classification of the answers.
- *Cross-case analysis.* As each of the cases had been analyzed comparison across the cases were made, to identify re-occurring patterns between the cases.

Findings

Findings from the studied cases are shortly summarized, reflecting our within-case analysis. We begin with summarizing the view of the clients and then the providers. The cases elaborate on reasons to outsource the experiences with service outsourcing.

Manufacturing Co. – Client

Manufacturing Co. wanted to realize savings, and the way forward was first to close local HR departments, and second to centralize and later outsource their HR department. The outsourcing included payments, recruiting, career plans and training. The experience was that the need for local adaptations and knowledge of the specific local situation is not always taken into account. For instance, in the process there were several complaints from local units that the centralised unit did not understand their needs, took too long to handle minor issues, and that the overall service quality was low.

The decision to centralize and outsource the HR department was countered locally by informally performing some of the HR tasks locally in other units, sometimes done by the same persons that now had new functions. One example is when a new employee was needed, but the formal recruiting process was considered too slow and cumbersome. Recruiting was done locally, in breach with company procedures. The reason for this was that the outsourced function “*did not understand our situation, and it would take longer to explain this to them than doing it our self*”.

Global Bank A – Client

Global Bank A is constantly scanning the internal organisation for activities that can be centralised and offshored to low cost locations and in the end maybe also outsourced. On transferring of knowledge, explicit knowledge is prioritised. This is done by an internal task force unit called “*the hunters*”. Global Bank A’s own estimation is that 10 percent of all tasks can be outsourced, or done in shared service centres, located in low-cost countries. The main driver for this is cost cutting, delivering the same quality to a lower cost. One of their main criteria’s when they examine a task for potential outsourcing is that there should be a written work description and training material for new personnel present, as detailed as possible. The focus is on explicit knowledge and formalised routines. When a task is transferred, work descriptions and formalised routines are used as a main tool in the transfer process.

Global Bank B – Client

Global Bank B has extensive experience in outsourcing and offshoring back office services. A rule of thumb shared by one manager in that they internally calculate that approximately 10-20 percent of the amount of resources used in the outsourced function is needed to manage the relationship with the provider. An observation made by the manager is that “*this is not necessarily the same persons; the skill to perform the task is not the same as the skill to manage the relationship with a provider*”. Managerial skills, negotiation skills and an ability to handle problems and improvements between the two organisations requires a different set of capability than to perform the task, or to manage a in-house team performing the task.

Regional Bank A – Client

Regional Bank A works actively with the centralisation of service functions to common central units within the bank. In total, 12% of all employees work in one of these service units. This has increased over the last years. The advantages according to the bank management are both cost reduction and a quality improvement in the service. Regional Bank A has chosen to centralise internally first, and may in a later stage consider outsourcing parts of the service. A more likely development is said to be that the bank may place some service units in low cost countries in the nearby region, as captive service units. Part of the service functions are also seen as being of strategic importance to the bank, such as customer contact units, and will not be outsourced due to this.

Offshoring Co. – Provider

Offshoring Co. describes itself as “*a production unit*”, where “*standard service components are produced for several clients*”. This view signifies the standardisation and industrialisation of the service production. A consequence of this is that any preferred adaptation to local needs in the client company is in conflict with the efficiency of the provider’s mass production of the service. The provider’s main competence is efficiency in producing the service, by reducing costs. Adaptations and improvement of the service to fit local needs is sometimes in conflict with this, as one provider states it “*we cannot make everyone happy, we need to set a standard*”. This focus on volumes and efficiency is also evident in marketing material from several service outsourcing providers. One uses the phrases “*industrial methods*” and “*service factories*”, while others emphasise their large offshore production centres.

Call Centre Co. – Provider

Call Centre Co. is a company showing resemblance with several other call centres we've come across in other studies. All call centre companies have a well developed IT-based production system. The system normally enables an extensive logging of the performed tasks, and a detailed follow up on each agent, down to a second-to-second level. What gets measured is data that is quantifiable, and by definition also explicit. Service level agreements, or SLA's, focus on quantified parameters such as response time, time to close an issue, and other time-related parameters. Even though some activities are of a more complex character, such as help-desk or technical support units, there is a strong culture of measuring quantitative aspects of the performed tasks. The work environment is similar to that of a production line, repetitive tasks with short cycle time. Many performed tasks are of an off-the-shelf character, short routine tasks, lasting less than 2 minutes, and formalised in scripts shown on the call centre agents screen. *"Quality is of course important, but a lot of the follow up is on calls per hour, and response time. It is easier, since it is more precise, and we have all figures from the system"*. There is a claim in many of the call centres that they also work with client satisfaction and quality related parameters, but generally this is done on a less frequent basis, and not used in the same way in daily follow up.

Much of the daily communication between clients and Call Centre Co. it is managed on an operative level. At Call Centre Co. the team leaders are in contact with their clients many times a day. Minor issues or problems are handled by first line managers, and in this way many issues are resolved in an informal manner. There are escalation procedures for *"real issues"*, but these are *"not a good way to handle problems"*. The communication works the best when the client has parts of the tasks outsourced and parts in-house. In this case *"there is someone to talk to that understands our problems"*. In some of the service outsourcing relationships there are no in-house activity left at the clients premises. This is seen as *"more problematic, since we don't have anyone to talk to in the same way"*.

Service Co. – Provider

Service Co., is working with a formal program for implementing Lean Production ideas on services. As a part of this the processes of the outsourcing clients is mapped, and a formal work description is produced, down to a detailed level. This is then used as training material for new personnel. The idea was that this detailed and formal process description should be used as a daily tool, but it turned out that most employees found it too detailed and hard to work with. This resulted in other ways to gain knowledge, where the most popular ones were to simply ask your colleague. New informal ways of *"how we do things"* were quickly established in the work groups at Service Co.

Department Co. – Provider

Department Co. takes a somewhat different aspect on service outsourcing as they take over entire departments from their outsourcing clients in the service outsourcing deal. These departments are then to be integrated in the outsourcing provider's organisation and way of working. This process has involved unlearning *"the way we do things around here"*. Thus, there is a challenge

to merge the culture of the outsourcing client with the more production oriented culture at Department Co. The aim is to increase productivity in the outsourced units, which has called for new ways of working. Service production know-how from Department Co. is applied on the outsourced unit. Experience shows that Department Co. sometimes go too far in focusing on the productivity of a particular unit, at the expense of understanding the effectiveness of this unit and is functioning in the outsourcing client's organization.

Major themes in the findings

Service outsourcing is influencing knowledge in several ways, both for the client and the provider. Through our cross-case analysis of the cases it is possible to identify three major changes as service outsourcing is conducted. First, there is a change of relative importance of knowledge types. There is an increased emphasis on explicit knowledge. This is caused partly due to the transfer situation and partly due to a focus on efficient mass production and a standardisation and industrialisation of the service. The focus on explicit knowledge leads to a loss of tacit knowledge. Below, we elaborate on these themes: (1) emphasis on explicit knowledge due to transfer, (2) emphasis on explicit knowledge due to standardization, and (3) loss of tacit knowledge.

Emphasis on explicit knowledge due to transfer

The focus on explicit knowledge is evident both in the actual knowledge transfer process when service outsourcing is initiated and tasks are transferred from the client to the provider, and also in the follow-up procedures when service outsourcing is in place.

At Service Co. there is an emphasis to produce formal work descriptions, down to a detailed level, which is used as training material for new personnel. Constantly this training material is being up-dated. However, the emphasis on explicit knowledge was seen as obsolete during a few initial months, since updates were too cumbersome to take part of. As a consequence an alternative update system built on short e-mails was used. Thus, the knowledge from the outsourcing client was first explicit, then transferred, then reworked to fit with the culture at Service Co., and when employees at Service Co. became more proficient with their tasks, shortcuts were developed and spread informally, still emphasising explicit knowledge.

From the description above it is suggested that in a service outsourcing relationship there is an increase focus on explicit knowledge both in the actual knowledge transfer process when work is being transferred from the client to the provider, but also in the relationship following. Below we elaborate on the actual transfer situation and the providers focus on efficient mass production and their attempt at standardizing and industrializing of the service, and how that affects knowledge transfer in general and the focus on explicit knowledge.

Emphasis on explicit knowledge due to standardisation

Several of the cases bear explains why there is an increased focus on explicit knowledge. The main reason is the providers attempts at standardize the tasks as much as possible to be able to specify and measure the result of their own work to enhance possibilities for improvements, but

also to report back to the outsourcing client about how work is going. Thus, there seem to be an underlying attempt to show that efficiency goals have been reached.

For instance, Service Co. tries to capture and formalize knowledge on a detailed level, which can be written down and documented, making follow-ups easier. Call Centre Co. reveals a similar pattern. Call Centre Co. measures everything that can be made measurable. However, attempts are being made to capture satisfaction of the client. Call Centre Co. also believes that other soft issues will become more important in the near future.

Loss of tacit knowledge

The result of the focus explicit knowledge in the process of transferring knowledge, i.e. tasks from the client to the provider means that tacit knowledge is lost. In the cases we could identify that when tasks were transferred, some of the activities performed by the in-house personnel were not fully identified due to difficulties to clearly specify all the details of a task being transferred.

These “fuzzy edges” of the transferred task, which are not accounted for, had for instance in Manufacturing Co. resulted in not only lower service levels, but also more work for the remaining organisation, and a less efficient execution of the task. Previously the tacit knowledge of the in-house personnel made it possible to cut corners and solve problems informally, which is difficult in an outsourced unit. In Manufacturing Co. the residual parts of the tasks in the HR function, were not captured and transferred to the provider, causing the local organisation to keep doing the entire task, for better quality and local adaptation. Thus, not only are important areas of knowledge are lost, since it is not transferred and not kept alive, but also it is costly as the local organization continues doing work it shouldn't.

If we view the problem of transferring tacit knowledge from the perspective of the provider, here using Offshoring Co. as the example, we see the reason. Offshoring Co. has an explicit focus on standardisation of processes. Clearly stating that they are not interested in tacit knowledge at the provider's local site, but only on what they can measure.

As is being described tacit knowledge is largely lost in the knowledge transfer process, or at least not transferred to the production site at the provider. One reason is that in service outsourcing relationships the idea is to implement new ways of performing the task, using improved systems. This has the effect that the old knowledge is sometimes seen as just that “old knowledge”, and discarded. As a consequence knowledge that is linked to individuals in the client organisation, and that is not encoded, is likely to be lost. In most of the cases we studied this knowledge were not transferred to the new production units at the provider.

Implication of a shift in requirement on staff

From the discussion above it is concluded that the type of knowledge needed is changed both for the client and the provider. For the client, to manage the relationship with an external provider a new set of relational and contractual skills is needed. This will require different personal skills, which can be a challenge, since employees may remain the same. The formerly important skills of performing the task, or the explicit knowledge of routines and procedures is replaced by other

types of skills. We can see that in Global Bank B the demands on the residual organisation are different than these on the outsourced function.

Another example can be found in Offshoring Co. where the provider focuses on the operational aspect of the task, with standard production procedures. The outsourcing clients, while ridding themselves of the actual performance of the task, needs other skills to adapt to the standardised delivery of mass produced low cost services.

Implication on different knowledge types

As stated above the purpose of the paper is to identify changes in and changed relationship between different types of knowledge in a service outsourcing relationship. Above we have identified and discussed that in a service outsourcing relationship there is an emphasis on explicit knowledge due to demands on standardization, resulting in a loss of tacit knowledge. This has implications for the knowledge both at the client and the provider. Below we elaborate on these implications and their effects for both parties in the relationship.

- Explicit knowledge in documented forms such as books, manuals, and software, plays a central role in all our studied cases. In all our cases the number one priority to manage knowledge in the service outsourcing relationship it is the ability to handle the process of explicit knowledge transfer. The emphasis of standards, routines and efficiency, linked to the need to clarify knowledge when transferring tasks between organisations and sites has given explicit knowledge a central position in the relationship.
- Tacit knowledge that resides in systems, routines and formal procedures is suffering from a transfer of tasks between a client and a provider. According to Lave J. & Wenger E. (1991) the reason for changes is that situated knowledge, or local knowledge, is knowledge that is dependent on the context in which it is situated. When the context is removed, the knowledge will lose part of its relevance, and thus lacks a generalised character, and over time new knowledge will emerge.
- Our analysis shows that the tacit knowledge at the client is most likely not transferred, but replaced by new tacit knowledge in the organisation of the provider. It is interesting to note that existing tacit knowledge related to the provider's local settings, personal relationships and organizations characteristics is changed. The reason is that both context and persons are changed in a service outsourcing relationship. As a paradox it is often exactly this knowledge is often needed to provide a high-quality service. This represents a problem seen for instance in Manufacturing Co., where knowledge on "how things work", or informal ways of fixing issues are lost when the service is outsourced. As Koners & Goffin (2007) point out; the tacit dimension of knowledge is often poorly understood.

Discussion

Service outsourcing may seem appealing at a glance, not least given the fact that research has shown a 10-20 percentage saving on measured factors (Clegg, 2005). Still, it is challenging engaging in service outsourcing as service quality may be reduced, and there can be a lack of cost savings due to increased management costs, and as low as 5 percent of all companies actually achieve significant benefits from outsourcing (Lonsdale, 1999; McIvor, 2000). From our

study one reason for failure to fully succeed in a service outsourcing relationship may be attributed to the attention given to explicit knowledge, at the expense of tacit knowledge.

A related challenge facing companies outsourcing services is the risk that the knowledge lost in the transfer of tasks in a service outsourcing deal may have negative effect. Outsourcing of a service may decrease the company's ability to solve problems informally. Persons with tacit knowledge are given new roles, or may leave the company, and the informal ways in which problems were solved cease to exist, which creates difficulties. This is a challenge that is very hard to put any figures on this, and thus it is often left out of the calculation. Consideration about informal solutions and tacit knowledge and how these can effectively be transferred needs to be taken more into account in service outsourcing decisions. Thus, the cost of developing new management competencies and capabilities is not only done at high risk, it may also be costly (Harland, et al., 2005)

The decreased level of operational knowledge in the client organisation is natural, if the maturing market of suppliers of standard services is taken into account. This links to the need for domain expertise needed at the providers discussed by Feeny et al. (2005). On the other hand, in the areas where the service providers are less mature, and the service offers are less standardised and developed, the requirements are higher on the outsourcing client. There is a risk that the client may rid themselves of the operational knowledge too soon. With only one or few suppliers available, this causes dependencies, and with immature suppliers, it will cause problems in defining and developing the services required.

Taking into account our research and previous research on service outsourcing we see two distinct ways to go to create a working service outsourcing relationship. One towards standardised, off the shelf task and a market based relationship. Service outsourcing is becoming more similar to component suppliers in manufacturing, where standardisation is taken a long way, and component suppliers may be producing identical parts, and may be interchanged easily. There is still some way to go in this aspect, but there is a movement towards commoditised services and off the shelf solutions. This is the logic found among our cases in this study. There is a focus on formal, measurable aspects of the relationship, condensed in the SLA. The observed process of standardisation and commoditisation further increases the market mechanisms and weakens the partnership aspects of the relationships.

The other way is towards services adapted to local needs and with a longer term partnership relationship. Both Willcocks (2004) and Barthelemy (2001) stress the importance of a closer relationship between the client and the provider. We have, however, seen very few examples of this approach both in practice and in the literature. Even though it may seem appealing it is still a challenge trying to implement this type of long-term relationship as the market is yet immature for many services. The outsourcing clients may be tempted to use market mechanisms in a situation where a longer term approach is more suitable, and thus creating a relationship where neither part is happy.

Conclusions

Our study's main contribution to the literature on service outsourcing and knowledge transfer is the following: we highlight that in a service outsourcing relationship the emphasis is most often on explicit knowledge. This is beneficial in a transaction cost relationship with standardized tasks being transferred. However, the more complex tasks being transferred the more difficult it is to clearly specify what is going to be transferred as the knowledge becomes more tacit, calling for more long-term relationships with other mechanisms for knowledge transfer in place. Furthermore, it was found that:

- In a service outsourcing relationship the relative importance of explicit knowledge is emphasized at the expense of tacit knowledge. The main reason being that it is hard to define, and later measure, the transfer of tacit knowledge.
- The focus on efficiency goals also stimulates thinking in terms of mass production and standardization and industrialization of a service, furthermore underlining the emphasis on encoded, explicit, knowledge. This in term may result in a loss of unwritten and local knowledge, i.e. tacit knowledge.

An implication for managers from both the client and the provider is that they need to acknowledge what type of tasks they are outsourcing, standardized and simple, or analytical and complex. A more complex relation between the parties, involving the outsourcing of functions rather than tasks, requires more interaction, and also more knowledge of the client's internal processes. This is not suited for a market relationship, but will more often lead to the establishment of a long term partnership. Depending on which type the relationship take is likely to affect the demands on knowledge sharing and interaction. A long term relationship with complex interaction requires other skills from both parts than a market based relationship with off the shelf service components.

All outsourcing will lead to some loss of knowledge in the client organisation. Whether this is a problem or not depends on the circumstances, but it should be taken into consideration when an outsourcing decision is made. The loss of tacit and locally situated knowledge is hardest to capture, but may in some cases have a long term effect on perceived quality and service level.

Limitations and recommendations for future research

As with all exploratory, this study has significant limitations, and more research is clearly needed in order to validate our findings. The limitations stem from several categories. We have chosen to study two countries, and more research is needed in countries with different characteristics. Another limitation is the small sample. Hence, for future research should also do survey-type research. For future research we suggest an attempt at going deeper into examining service outsourcing aiming at being long term and adapted to local needs trying to identify what the critical success factors are and what may hinder such a relationship.

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Appendix

Table 1: Summary of the 8 companies studied

Case study no.	Employees	Industry	Presence	Provider or Client
1. Manufacturing Co.	>50.000	Consumer Goods	Global	Client
2. Global Bank A.	>100.000	Banking	Global	Client
3. Global Bank B.	>100.000	Banking	Global	Client
4. Regional Bank A.	30.000	Banking	Europe	Client
5. Offshoring Co.	5.000	Various; accounting, data entry, back office administration	South East Asia	Provider
6. Call Centre Co.	10.000	Call centre provider, with English as main language	South East Asia	Provider
7. Service Co.	5.000	Various, call centre, third part logistics provider, HR provider	Europe	Provider
8. Department Co.	3.000	Various, outsourcing / outplacement takes over and runs entire departments	Europe	Provider